Supreme Court, U.S.
FILED

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No.

IN THE

Supreme Court of the United States

Jesse and Marjorie Rupert,
Petitioners

v.

Commissioner of Internal Revenue,
Respondent

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRUIT

PETITION FOR WRIT OF CERTIORARI

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59

QUESTIONS PRESENTED FOR REVIEW

1. Under Section 7491(a) of the Internal Revenue Code, isn't a taxpayer entitled, in a court proceeding, to have the burden of proof automatically shifted to the Commissioner when he introduces credible evidence with respect to any fact issue relevant to determination of his tax liability?

2. What constitutes credible evidence and how does a taxpayer meet the burden of introduction of credible evidence under Section 7491(a) of the Internal Revenue Code?

3. Are the Limitations of Section 7491(a)(2) of the Internal Revenue Code met by taxpayer's upon exhaustion of administrative remedies or the receipt of a

Notice of Deficiency or does it continue through trial?

4. Under Section 162 of the Internal Revenue Code, is a taxpayer not entitled to deduction of ordinary and necessary business expenses regardless of whether it was incurred on behalf of a family member?

5. Is the taxpayer not entitled to a shorter depreciation deduction, on a converted property, placed in service in 1986, but deducted in 1991, under Sections 167, and 168(3) of the I.R.C.?

6. Under Section 6664(c) of the I.R.C., is the taxpayer not entitled to a waiver of penalties if the taxpayer shows reasonable cause and that he acted in good faith?

LIST OF PARTIES IN COURT BELOW

1. Jesse and Majorie Rupert, Petitioners
2. Commissioner of Internal Revenue,

   Respondent

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ON PETITION FOR A WRIT OF CERTIORARI TO

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FOR THE FIFTH CIRUIT

PETITION FOR WRIT OF CERTIORARI

Jesse and Marjorie Rupert, petitioners herein, respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of

Appeals for the Fifth Circuit, enter in the above-entitled case on January 9, 2003.

CITATION OF OPINIONS AND ORDERS IN CASE

The opinion of the Court of Appeals, whose judgment is herein sought to be reviewed is Case Number 02-60101, dated January 9, 2003, (Not Published), is reprinted as Appendix 1.

The prior opinion of the United States Tax Court, entered on February 11, 2002 is reported at 82 T.C.M. 197, is reprinted as Appendix 2.

JURISDICTIONAL STATEMENT

The judgment of the United States Court of Appeals for the Fifth Circuit was entered on January 9, 2003. Petitioner filed a Petition for Rehearing and Rehearing En Banc. The court below entered an order (reprinted as Appendix 3) denying the petition on April 8, 2003.

This petition is filed within 90 days of that date, so this Court has jurisdiction to review the judgment of the Fifth Circuit on petition for certiorari pursuant to 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The relevant statutory provisions involved are IRC Sections 7491(a), 162, 167, and 6664(c)(1), reproduced verbatim as follows:

§ 7491. Burden of Proof

> **a. Burden shifts where taxpayer produces credible evidence. --**
>
> **(1) General rule.** —If, in any court proceeding, a taxpayer introduces credible evidence with respect to any factual issue relevant to ascertaining the liability of the taxpayer for any tax imposed by subtitle A or B, the Secretary shall have the burden of proof with respect to such issue.

(2) Limitations. –Paragraph (1) shall apply with respect to an issue only if—

i. the taxpayer has complied with the requirements under this title to substantiate any item;

ii. the taxpayer has maintained all records required under this title and has cooperated with reasonable requests by the Secretary for witnesses, information, documents, meetings, and interviews; and

iii. in the case of partnership, corporation, or trust, the taxpayer is described in section 7430(c)(4)(A)(ii).

Subparagraph (C) shall not apply to any qualified revocable trust (as defined in section 645(b)(1)) with respect to liability for tax for any taxable year ending

after the date of the decedent's death and before the applicable date (as defined in section 645(b)(2)).

(3) Coordination. –Paragraph (1) shall not apply to any issue if any other provision of this title provides for a specific burden of proof with respect to such issue.

Sec. 162. **Trade or business expenses.**

(a) In general.

There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including –

(1) a reasonable allowance for salaries or other compensation for personal services actually rendered;

(2) traveling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the

circumstances) while away from home in the pursuit of a trade or business; and

(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

Sec. 167. Depreciation.

(a) General rule.

There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

(1) of property used in the trade or business, or

(2) of property held for the production of income.

§ 6664

(c) Reasonable cause exception.

(1) In general. No penalty shall be imposed under this part with respect to any portion of an underpayment if it is shown that there was a reasonable cause for such portion and that the taxpayer acted in good faith with respect to such portion.

STATEMENT OF THE CASE

Respondent, after an examination, denied petitioners' business expense deduction, depreciation deduction and accessed an accuracy related penalty on petitioners 1996 income tax return.

In 1987, petitioners retired and returned from overseas to their residence in League City, Texas. Their sources of income subsequently were from IRA accounts, social security and consulting work.

Petitioner, Jesse, started his consulting business in 1987 after retirement. Said business generated income in 1991 and was reported on his tax return. In 1996, as part of his consulting business, he entered into an agreement with his daughter, Michelle Ann Steele who was involved in a custody case in California. In consideration for paying her legal, medical and other expenses associated with her case, petitioner, Jesse was to receive 30 percent of gross recovery after expenses. Recovery was estimated to be over $700,000.00. Petitioner, Jesse withdrew $30,000.00 from his IRS account to fund the agreement. In 1996, petitioners incurred and deducted $37,310.00 in business expenses associated with the agreement. Respondent denied the deduction. Petitioners were also denied a depreciation deduction in 1996 on a mobile home that they purchased in 1982 and converted it to property held for production of income in 1986, but started

taking depreciation in 1991, when it was first rented. Furthermore, petitioners were assessed an accuracy related penalty. Petitioners after exhausting the appeals process, petitioned the United States Tax Court, after they received a Notice of Deficiency.

The District Court Decision

Petitioners filed a complaint with the United States Tax Court disputing the denial of the deductions and penalty assessment. At trial, petitioners testified about how they met the requirements of Section 7491(a), I.R.C., when he placed his mobile home for production of income in 1986, but did not start taking depreciation until it was rented in 1991. The tax court ruled that petitioners had the burden of proof as to the business expense deduction, that petitioner's mobile home was placed in service in 1991 and not 1986 and thus, entitled to 27.5 years depreciation instead of 10 years. Moreover, despite petitioners testimony about their

reliance on their research, review of IRS materials and consultation with an attorney prior to preparing their 1996 tax returns, the tax court found them liable for an accuracy related penalty.

The Court of Appeals Decision

The Fifth Circuit affirmed the Tax Court's decision after hearing oral argument. However, their decision was silent as to who had the burden of proof at trial, though the issue was briefed.

Existence of Jurisdiction in Courts Below

This action was commenced in the United States Tax Court. The tax court had jurisdiction pursuant to I.R.C. §§ 6213,6214 and 7442. The final judgment of the tax court was entered on February 11, 2002. Timely appeal was filed to the United States Court of Appeals for the Fifth Circuit, which had jurisdiction over the matter under 28 U.S.C. § 7482(a).

ARGUMENT FOR GRANTING THE WRIT

1. **I.) THE ISSUE OF WHEN DOES THE BURDEN OF PROOF SHIFT UNDER SECTION 7491(a), I.R.C, HAS NOT BEEN SETTLED BY THIS COURT**

The failure of the Fifth Circuit to address the issue of the burden of proof completely ignores the sole purpose of Section 7491a, I.R.C., "Taxpayer Bill of Rights 3." Said Section took away the presumption of correctness afforded the Commissioner and analogized it to our criminal law system where the government has to prove you guilty. Senator Gramm sums it up that under existing tax law, you are guilty until you prove yourself innocent. Senate Floor Debate For Amendment No. 2374(144 Cong. Rec. 56, S4484)

Petitioners testified at trial about their several meetings with the I.R.S. through appeals. Petitioners Exhibits regarding business expenses and

depreciation deduction were stipulated to and admitted into evidence. Despite all the foregoing the Fifth Circuit agreed with the Tax Court that petitioners have the burden of proof.

This Court should review and reverse the decision below because it ignores Section 7491(a), I.R.C. and it takes away a Bill of Rights given to taxpayers.

II.) THE FIFTH CIRCUIT'S DECISION THAT AFFIRMED THAT THE TAXPAYER HAS THE BURDEN OF PROOF IS IN CONFLICT WITH THE DECISION OF THE EIGHT CIRCUIT

Contrary to the Fifth Circuit, in Griffin v. Commissioner of Internal Revenue, 315 F. 3d 1017 (8th Cir. 2003), that court found that the Commissioner of Internal Revenue Service has the burden of proof regarding deductibility of tax payments. Guidance by this Court is needed regarding the application of Section 7491(a), I.R.C. to help resolve conflicts between the Circuits and to

protect the Taxpayers Bill of Rights. This case should be reversed and remanded for further proceedings given that the commissioner now has the burden of proof.

2.) **THE ISSUE OF WHAT CONSTITUTES "CREDIBLE EVIDENCE" AND HOW THE BURDEN IS MET UNDER SECTION 7491(a), I.R.C. HAS NOT BEEN SETTLED BY THIS COURT, NEITHER DOES THE CODE DEFINE "CREDIBLE EVIDENCE"**

The Code does not define the term "credible evidence." However, the legislative history defines the term "credible evidence" as "the quality of evidence which, after critical analysis, the court would find sufficient upon which to base a decision on the issue if not contrary evidence were submitted (without regard to the judicial presumption of I.R.S. correctness)." H.R. Conf. Rep. No. 105-599, at 240-241 (1998), 1998-3C.B. 747, 994-995. The Court in Griffin adopted the above definition of "credible evidence," however, it left open the question how a

taxpayer can meet the burden of introducing credible evidence to shift the burden of proof. This issue is of paramount importance, as it will affect any tax court litigation, at minimum.

The failure of the Fifth Circuit to address the issue of whether petitioners introduced credible evidence, despite petitioners overwhelming evidence, ignored the petitioners' Bill of Rights and requires guidance and a reversal by this court.

3.) **THE ISSUE OF WHETHER THE LIMITATIONS OF SECTION 7491(a)(2), I.R.C. ARE MET BY EXHAUTION OF THE ADMINISTRATIVE REMEDIES OR WHETHER IT STOPS AFTER RECEIPT OF A NOTICE OF DEFICIENCY OR WHETHER IT CONTINUES THROUGH TRIAL HAS NEVER BEEN SETTLED BY THIS COURT.**

The limitations of Section 7491(a)(2), I.R.C. is the basis for application of Section 7491(a)(1). Unfortunately there is not authority as to whether the substantiation, record maintenance, cooperation with requests for information, etc., are met by the

taxpayers exhaustion of administrative remedies, or whether it stops after receipt of a Notice of Deficiency or whether it continues through trial.

The Fifth Circuit's failure to address this issue in essence says that section 7491(a), I.R.C. is not applicable in this case. A reversal is necessary to uphold the Taxpayers Bill of Rights.

4.) I.) **THE FIFTH CIRCUIT'S DECISION THAT AFFIRMED THE TAX COURT DECISION DENYING DEDUCTION OF PETITIONERS' BUSINESS EXPENSES IS CONTRARY TO PRINCIPLES ESTABLISHED BY THIS COURT.**

Taxpayers who pursue an activity full-time, in good faith and with regularity, and produce incomes, and that is not merely a hobby, are thus engaged in a trade or business. Commissioner v. Groetzinger, 480 U.S. 23 (1987). Moreover, a taxpayer has a right to arrange his affair so as to minimize the taxes he pays. Gregory v. Helvering, 293 U.S. 465, 55 S. Ct. 266, 267, 79L. Ed. 596 (1935)

At trial, Respondent's dispute was that petitioners were not engaged in a business rather than the amount of the business deduction, as petitioners business expenses were stipulated to. Moreover, Respondent conceded other business expenses of petitioners. Despite the foregoing and petitioners evidence, the Fifth Circuit affirmed the tax court denial of petitioners business expenses.

The Fifth Circuit's decision is contrary to the foregoing cases of this court and requires reversal because petitioners proved that they were engaged in a trade or business and Respondent offered no contradicting evidence.

5.) THE DENIAL OF DEPRECIATION DEDUCTION UNDER THE ACRS WHICH PROVIDES FOR A 10 YEAR TAX LIFE IS CONTRARY TO RESPONDENT'S OWN RULES AND REGULATIONS

Under the Accelerated Cost Recovery System (ACRS), manufactured homes have a 10-year useful

life if placed in service before 1987. See Former Section 168(n)(3), Pub. L. 99-514, 110 Stat. 2085. Modified Accelerated Cost Recovery System replaced ACRS and provided a 27.5 years useful life for property placed in service after December 31, 1986. Tax Reform Act, Pub. L. 99-514, § 203(a)(1)(A). The issue in this case was when was the property placed in service. An asset is considered placed in service when it is in a condition or state of readiness and availability for a specifically assigned function, and depreciation period begins when an asset is placed in service and ends when it is retired from service. I.R.C. Regulations, section 1.167(a)-10.

The petitioners testimony and uncontradicted evidence is that their mobile home was placed in service in 1986 when they converted it to property held for appreciation/production of income. However, they started taking depreciation deduction in 1991, after it was rented. Petitioner's depreciation

deduction complies with the foregoing Regulations and requires a reversal.

6.) **THE DECISION BELOW IS IN CONFLICT ON THE ACCURACY-RELATED PENALTY ISSUE WITH THE NINTH CIRCUIT AND THE I.R.C. SECTION 6664(c).**

I.R.C. Section 6664(c) provides for a waiver of the penalties under Section 6662 if tax payers can show that he had reasonable cause and acted in a good faith. In Betson v. Commissioner, 802 F.2d 365,372(9th Cir. 1986), the court found that taxpayer's reliance on his accountant's advice constituted reasonable cause and good faith under Section 6664(c).

Evidence on this case on this issue consisted solely the uncontradicted petitioner, Jesse testimony about how he relied on his research, IRS publications and the advice of his attorney in preparing his 1996 tax return. The Fifth Circuit affirmance of the tax

court's decision clearly conflicts with the Betson case and I.R.C. Section 6664(c), and requires reversal.

CONCLUSION

For all the foregoing reasons, petitioners respectfully prays that this petition for writ of certiorari be granted.

Respectfully Submitted,

Jesse Rupert
Marjorie Rupert

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Certificate of Service

I hereby certify that a copy of this petition for writ of certiorari was mailed by certified mail, return receipt requested on November 13, 2003, to Respondent's attorney of record:

Sarah Ann Ketchum
U.S. Department of Justice
P.O. Box 502
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Respectfully Submitted

Jesse Rupert

Jesse Rupert

APPENDIX

1. Court of Appeals opinion and judgment
2. United States Tax Court decision and judgment
3. Order denying petition for rehearing

Appendix 1

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 02-60101

JESSE EMMIT RUPERT AND MARJORIE A. RUPERT,
Petitioners-Appellants
v.

COMMISSIONER OF INTERNAL REVENUE
Respondent - Appellee

Appeal from a Decision of the United States Tax Court

Before BENAVIDES and DENNIS, Circuit Judges, and WALTER, District Judge.*

PER CURIAM.**

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*District Judge for the Western District of Louisiana sitting by designation

**Pursuant to Fifth Circuit Rule 47-5, the Court has determined that this opinion should not be published and is not precedent except under the limited circumstances set forth in Fifth Circuit Rule 47-5.4.

In this appeal, plaintiffs-appellants ("Taxpayers") argue that the Tax Court clearly erred in determining that (1) Taxpayers were not entitled to deduct, as business expenses, legal expenses incurred by their daughter, but paid for by Taxpayers, in her domestic relations litigation; (2) Taxpayers were entitled to a depreciation deduction on their mobile home but the depreciation was to take place over a longer tax life than that used by Taxpayers; and (3) Taxpayers were liable for the accuracy-related penalty in I.R.C. §6662(a) with regard to the portion of the underpayment attributable to Taxpayers' claim of the deduction for legal and professional fees.

After carefully considering the briefs and the positions advanced at oral argument, it is clear that the record reflects that Taxpayers' daughter's legal expenses incurred as a result of divorce proceedings were not ordinary and necessary business expenses attributable to Mr. Rupert's engineering consulting

business. Thus, these expenses were not deductible. Furthermore, for the reasons stated by the Tax Court, it was correct to impose an accuracy-related penalty for deduction of these expenses.

Finally, the record is clear that Taxpayers' mobile home was not placed in service as rental property until 1991. Thus, the Tax Court was correct in finding that Taxpayers were entitled to a 27.5-year depreciation deduction under the modified accelerated cost recover system for their mobile home, rather that the 10-year depreciation deduction available for rental property placed in service on or before December 31, 1986 claimed by Taxpayers. Tax Reform Act of 1986 ("TRA"), §203(a)(1)(A); Treas. Reg. §§ 1.167(a)-10(b) and 1.167(a)-11(e)(1)(i); Treas. Reg. §1.167(a)-11(e)(1)(i); Treas. Reg. §1.46-3(d)(1)(ii).

Accordingly, the Tax Court did not err in its findings. We therefore AFFIRM the judgment of the Tax Court.

U.S. COURT OF APPEALS

FILED: JAN 9, 2003

CHARLES R. FULBRUGE III
CLERK

Appendix 2

UNITED STATES TAX COURT

JESSE EMMIT and MARJORIE A. RUPERT Petitioners,	§	
vs.	§	Docket No. 11995-99
COMMISSIONER OF INTERNAL REVENUE, Respondent.	§	

DECISION

Pursuant to the opinion of the Court filed July 19, 2001, and incorporating herein the facts recited in the respondent's computation as the findings of the Court, it is

ORDERED AND DECIDED: That there is a deficiency in income tax due from the petitioners for the taxable year 1996 in the amount of $18, 676.00;

That there is a penalty due from the petitioners for the taxable year 1996, under the provisions of I.R.C. § 6662(a), in the amount of $2,130.80.

` Judge

Entered: Feb. 11, 2002

T.C. MEMO. 2001-179

UNITED STATES TAX COURT

JESSE EMMIT AND MARJORIE A. RUPERT, Petitioners v. COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 11995-99. Filed July 19, 2001.

Joseph Onwuteaka, for petitioners.

Elaine H. Warren, for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

GERBER, Judge: Respondent determined a $19, 136 deficiency and an accuracy-related penalty under section 6662 (a)[1] of $3,629 in petitioners' 1996 Federal income tax. After agreements of the parties,

[1]All section references are to the Internal Revenue Code in effect for the year in issue, and all Rule references are to the Tax Court Rules of Practice and Procedure, unless otherwise indicated.

the issues presented for our consideration are: (1) Whether petitioners are entitled to deduct certain legal expenses paid in connection with their daughter's domestic relations proceedings; (2) whether petitioners are entitled to claim depreciation deductions with respect to a rental residence and, if so, the amount of depreciation to which they are entitled; and (3) whether petitioners are liable for a section 6662 (a) penalty with respect to the legal expense issue.

FINDINGS OF FACT[2]

At all pertinent times, petitioners were married and resided in League City, Texas. Jesse Emmit

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[2] Because of the discrete nature of the facts and legal discussion for each issue, the findings of fact and legal discussion for each issue are separately set forth. The fact finding is being segregated for convenience only, and all findings are applicable throughout the opinion. The parties' stipulation of facts is incorporated by this reference.

Rupert (petitioner) retired from his position as a drilling manager for Atlantic Richfield Indonesia, Inc. (Atlantic Richfield), on February 1, 1987. Since his retirement, petitioner has been involved in investing and did a limited amount of engineering consulting during 1991.

In 1992, petitioners' daughter Michelle Ann Steele (Michelle) became involved in a divorce proceeding against her then husband, Tad Edward Wilkinson (Tad). When the proceeding was instituted, Michelle and Tad had a daughter, Ashley, who was about 2 years old. During the period 1992 through 1995, petitioner studied domestic relations law because he thought that Michelle was being "cheated", and he encouraged her to discharge her attorney. In 1995 a divorce was granted, and Michelle received primary custody of Ashley. Thereafter, by means of a legal proceeding, Tad sought primary custody of Ashley. In order to defend

against Tad's action, petitioner withdrew $30,000 from his retirement account to pay part of the legal and professional fees.

On April 20, 1996, petitioner and his daughter, Michelle, entered into a written agreement under which petitioner agreed to pay legal, medical, and other expenses incurred in connection with Michelle's claims against Tad in exchange for which Michelle agreed to pay petitioners 30 percent of any residual recovery received from Tad. The residual was payable only after payment of Michelle's and petitioner's expenses. At that time Michelle was indigent and without representation. On April 26, 1996, after consultation with Attorney Daniel Murphy, petitioners, through Attorney Murphy, intervened in the custody litigation between Michelle and Tad. By intervening, petitioners sought custody of their granddaughter Ashley. During October 1996, Attorney Murphy also began representing Michelle in

the custody proceeding. During 1996 petitioner incurred $39,274 for legal expenses including $26,691 in professional fees, $8,550 for travel, and $4,033 in office expenses.

During October 1996, custody of Ashley was granted to Tad, who was living in Saudi Arabia. Petitioner's only recovery under the agreement with Michelle was $1,920 recovered in 1999. As of the time of trail in this tax case, the divorce proceeding was still pending and, by its terms, the written agreement between petitioner and Michelle had terminated. Petitioners claimed the $39,274 as "Legal and professional services" on a Schedule C, Profit or Loss From Business, for "Rupert's Engineers", the principal business activity of which was shown as "consulting". No income from consulting was reported for 1996 and none had been reported since 1991, when $7,710 was reported. Petitioners' source of income since 1991 has been Social Security

payments, retirement accounts, and investments. Since execution of the agreement with Michelle, petitioner has devoted more than half of his time to Michelle's domestic relations problem.

OPINION

Ordinary and necessary expenses paid or incurred in carrying on a trade or business are deductible under section 162. Conversely, personal, living, or family expenses are not allowable. Sec. 262. The origin and character of the claim in litigation is determinative of whether litigation expenses are personal or deductible. United States v. Gilmore, 372 U.S. 39 (1963). In particular we look to whether the claim arose in connection with profit-seeking activity. Id. At 48.

Petitioners claimed $39,274 of legal, professional, and related expenses in connection with their daughter's divorce and custody litigation. We note that some portion of the claimed expenses

related to petitioners' attempt to gain custody of their grandchild. Petitioner argues that he was engaged in a full-time consulting business during the years under consideration and that his involvement in Michelle's divorce and custody proceedings was part of that endeavor. Respondent has countered that, as a preliminary matter, petitioner's consulting activity did not rise to the level of being a trade or business. Even if petitioner's consulting activity was a trade or business, respondent argues that the expenses paid in connection with Michelle's domestic relations litigation are not directly connected with or proximately related to petitioner's consulting activity. Finally, respondent argues that the origin and very nature of petitioners' involvement in their daughter's

domestic relations activity are personal. We agree with respondent that the expenses in question are not deductible.[3]

Petitioner retired from his position as a drilling manager for Atlantic Richfield during 1987 and after that time was paid on one occasion during 1991 for consulting in connection with his preretirement expertise. Other than the $7,710 consulting fee earned during 1991, petitioner had no active income-producing consulting engagements. See Commissioner v. Groetzinger, 480 U.S. 23 (1987).

Even if we were to find that petitioner's consulting activity reached the level of being a trade or business or other profit-seeking activity, we are

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[3] We need not decide whether sec. 7491(a) affects the placement of the burden of proof here, because we resolve the issues on the basis of a preponderance of the evidence in the record.

unconvinced that petitioners' involvement in their daughter's domestic relations difficulties was an integral part of petitioner's consulting activity. Although petition studied domestic relations law and related matters, he is not a lawyer and not entitled to represent the interests of another. In that regard, there was no potential for profit from "investing" in a divorce or child custody proceeding. Petitioners' assistance to their daughter is commendable, but it is in origin and character a personal matter.

Petitioner spent a great deal of effort in researching domestic relations law and assisting his daughter, but that alone does not make his activity one that is profit seeking. We also note that petitioner entered into an agreement with his daughter. Under that agreement, petitioner would be reimbursed for his expenditures pro rata, using the ration of his expenditures to his daughter's. Once their expenditures were reimbursed, then petitioner was to

receive 30 percent and his daughter 70 percent of any recovery that exceeded the cost of the domestic relations proceedings. Although petitioner personally calculated potential for recovery, he did not possess the background and expertise to lend credibility to such projections. There has been no showing that there was any potential for a recovery that exceeded the expenditures on behalf of the litigant; i.e., that Michelle would be entitled to alimony and or some form of damages that exceeded the amount of expenditures that Michelle and petitioner incurred in the proceedings. Even though there was a written agreement, in substance, petitioner was merely being a good parent and assisting his daughter in her time of need. In addition, petitioners were personally seeking custody of their granddaughter. On this record, we are unable to elevate this arrangement to a profit-seeking activity.

Accordingly, we hold that petitioners are not entitled to deduct the $39,274 expended in connection with their daughter's domestic relations litigation.

II. Depreciation

FINDINGS OF FACT

On July 11, 1982, petitioner purchased a 1982 mode, 28-foot mobile home for $36,000, and it was placed on a long-term leased lot on Lake Cherokee in Henderson County, Texas. Petitioners permanently affixed the home to the realty by removing the wheels and axles, placing it on foundations blocks, and securing it with steel straps attached to the ground anchors. Petitioners added certain other improvements in and around the home, including a 12- by 24-foot deck, a concrete perimeter, a storage area, electrical wiring, a water system, a boathouse, a deck, and an electric lift. The cost were stationed overseas until 1986, they used the home only occasionally for vacation during their infrequent visits

to the United States. Petitioner had a heart attack during 1986, and there was no further vacation use after 1985. When petitioner retired, petitioners purchased a residence in League City, Texas. On their 1991 through 1996 tax returns, petitioners reported the home as a rental property and reflected income and deductions on Schedules E, Supplemental Income and Loss. For each year depreciation approximating $3,900[4] was claimed on the Schedule E in connection with the home. Gross rents were reflected for 1991, 1993, and 1994 in the amounts of $1,782, $4,200, and $350, respectively, and no rents were reported for the years 1995 through 1998. The property was first rented in 1991 when its value was $39,000.

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[4] For reasons which are not explained in the record, petitioners claimed $3,900 in some years and $3910 in others. For the 1996 tax year, however, petitioners claimed $3,900.

OPINION

Respondent determined that petitioners were not entitled to $3,900 of depreciation on the home for 1996. Petitioners' Schedule E for 1996 reflected a $7,305 loss from rental of the home. That loss comprised the $3,900 claim for depreciation and $3,405 of other expenses, including utilities, land rent, etc. In his answer to the petition, respondent alleged "that, if the mobile home is held for the production of income, the property should be depreciated as 27.5-year class residential real property under MACRS [modified accelerated cost recovery system] rather than as 10-year property under ACRS [accelerated cost recovery system]."

The parties stipulated that the acquisition cost of the rental home was $36,000. At trail, petitioner's uncontroverted and believable testimony reflected that significant improvements were made to the home, including the removal of wheels and axles,

placing it on foundation blocks, securing it with steel straps attached to ground anchors, adding a 12- by 24-foot deck, a concrete perimeter, a storage area, electrical wiring, a water system, a boathouse, a deck, and an electric lift. In addition, petitioner's uncontroverted testimony was that the improvements cost $3,100.[5] Petitioner, as owner of the property, testified that the value of the home and the improvements was at least $39,100 in 1991, the first year it was rented. See sec. 1.167 (g)-1, Income Tax Regs. Petitioner testified that no depreciation was claimed or allowable before 1991. No evidence contradicted petitioner's testimony. Accordingly, there is sufficient and credible evidence in the record

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[5] Although petitioner testified that the cost of the improvements was $3,100, for 1996 the depreciation claimed was $3,900, which would indicate $3,000 rather than $3,100 of improvements. See also supra note 4.

to establish that petitioners' basis in the rental home was $29, 000 as of 1991.

We find that the property was held for the production of income during 1996 and that it was placed in service in 1991. Our findings are supported by petitioner's uncontroverted testimony reflecting his intent to rent or sell the property during 1996 and by the fact that it was rented during prior years. Respondent argues that the rentals and income reported from the property were received from a person related to petitioners. That fact, standing alone, does not show that the rental activity was not bona fide or that no profit was intended. There has been no evidence of petitioners' personal use after 1985. There has been no showing that the rentals were not at arm's length or that the amounts received were not based on fair rental rates.

Finally, respondent argues that petitioners must use a 27.5-year life in accord with MACRS.

Respondent admits that manufactured homes were treated under ACRS as having a 10-year life. Sec. 168(h)(3) (before the Tax Reform Act of 1986 (TRA), Pub. L. 99-514, 110 Stat. 2085). However, TRA sections 201, 203, and 211, 100 Stat. 2122-2123, 2143, established a 27.5-year life under MACRS for this type of property if it was placed in service after December 31, 1986. See Hosp. Corp. of Am. V. Commissioner, 109 T.C. 21, 42 (1997). Accordingly, the key here is the date when the property was placed in service. If it had been placed in service before 1987, then petitioners would have been able to elect the 10-year life.[6] The property was rented during 1991, 1992, and 1993. In that regard, petitioner testified that the property was placed in service in

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[6] We note that the returns available in our record date back only as far as 1991. If petitioners had placed the property in service before 1987 using a 10-year life, there would have been no basis left to depreciate as of the 1996 tax year.

1991, the first year that it was rented. Accordingly, the 10-year life cannot apply, and the depreciation must be based on a 27.5-year life. We leave the parties to compute the amount of depreciation allowable for the 1996 tax year.

III. Accuracy-Related Penalty

OPINION[7]

Respondent determined that petitioners were liable for an accuracy-related penalty under section 6662 with respect to the portion of the deficiency that is caused by any underpayment related to the $39,274 legal and professional fee deduction and the omission of the $30,000 withdrawal from petitioner's retirement account. Respondent did not apply the accuracy-related penalty to the $3,900 depreciation adjustment. Respondent, in his answer, conceded that

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[7] No specific finding is set forth here because the findings of fact set forth with respect to the legal and professional fees will suffice.

petitioners are not liable for the accuracy-related penalty with respect to the omission from income of the $30,000 withdrawal from petitioner's retirement account.

Section 6662(a) imposes a 20-percent accuracy-related penalty if any portion of an underpayment is attributable to negligence or disregard of rules or regulations or any substantial understatement of tax. Negligence is a lack of due care or failure to do what reasonable and prudent persons would do under the circumstances. Marcello v. Commissioner, 380 F. 2d 499, 506 (5th Cir. 1967), affg. in part and remanding in part on another issue 43 T.C. 168 (1964).

No penalty is imposed if it is shown that the taxpayer had reasonable cause and acted in good faith. Sec. 6664 (c). A taxpayer may be considered to have good faith or to be reasonable if he relied on his accountant or attorney and that reliance was

reasonable. See United States v. Boyle, 469 U.S. 241, 251 (1985). Petitioners contend that they relied on attorneys with respect to their pursuit of their daughter's domestic relations litigation, but there is no showing that petitioners relied on professionals for their reporting position where they claimed the $39,274 as expenses incurred in petitioner's consulting business. We note that petitioner prepared his own 1996 Federal income tax return.

Under section 7491 (c), respondent must carry the "burden of production" with respect to the question of whether petitioners are liable for penalties, including the accuracy-related penalty. See Higbee v. Commissioner, 116 T.C. ___, ___, (2001) (slip op. at 14). We have concluded that the burden of production required of the Commissioner is that he "must come forward with sufficient evidence indicating that it is appropriate to impose" the accuracy-related penalty. Id. at ___ (slip op. at 15).

There is sufficient evidence in this record to support our holding that respondent has met the above-described burden. Petitioners' very act of veiling their claim of expenses for their daughter's domestic relations litigation as part of an engineering consulting business shows that they acted negligently and not with good faith. Petitioners' reporting position gave the false impression that the $39,274 was being claimed in a Schedule C activity that was connected with "Engineering". In addition, petitioners' attempt to claim what are clearly personal expenditures as a business item supports the imposition of the penalty. Under these circumstances, we find petitioners liable for the accuracy-related penalty of section 6662 (a0 with respect to the portion of the underpayment attributable to their claim of the $39,274 of legal and professional fees.

To reflect the foregoing and the agreement of the parties,

Decision will be entered under Rule 155.

Appendix 3

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CCICUIT

No. 02-60101

JESSE EMMIT RUPERT; MARJORIE A RUPERT

Petitioners-Appellants

v.

COMMISSIONER OF INTERNAL REVENUE

Respondent-Appellee

Appeal of a Decision of the United States Tax Court

ORDER:

IT IS ORDERED that appellants' motion for leave to file petition for rehearing and petition for rehearing en banc out of time is ***Granted.***

FORTUNATO P. BENAVIDES
UNITED STATES CIRCUIT JUDGE

U.S. COURT OF APPEALS
FILED: MARCH 20, 2003
CHARLES R. FULBRUGE III (CLERK)

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CCICUIT

No. 02-60101

JESSE EMMIT RUPERT; MARJORIE A RUPERT

Petitioners-Appellants

v.

COMMISSIONER OF INTERNAL REVENUE

Respondent-Appellee

Appeal of a Decision of the United States Tax Court

ON PETITION FOR REHEARING AND
REHEARING EN BANC

(Opinion 01/09/03, 5 Cir., _____, _____, F. 3d _____)

Before BENAVIDES and DENNIS, Circuit Judges,

and WALTER, District Judge.*

PER CURIAM:

( ) The Petition for Rehearing is DENIED and no

member of this panel nor judge in regular active

service on the court having requested that the court be polled on Rehearing En Bank, (FED. R. APP. P. and 5th Cir. R. 35) the Petition for Rehearing En Banc is also DENIED.

( ) The petition for Rehearing is DENIED and the court having been polled at the request of one of the members of the court and a majority of the judges who are in regular active service not having voted in favor, (FED. R. APP. P. and 5th CIR. R. 35) the Petition for Rehearing En Banc is also DENIED.

( ) A member of the court in active having requested a poll on the reconsideration of this cause en banc, and a majority of the judges in active service not having voted in favor, Rehearing En Banc is DENIED.

ENTERED FOR THE COURT:

_____

United States Circuit Judge

*District Judge for the Western District of Louisiana sitting by designation.

U.S. COURT OF APPEALS
FILED: APRIL 8, 2003
CHARLES R. FULBRUGE III
CLERK